

BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 2013-199-WS

IN RE:)
)
Application of United Utility Cos., Inc,)
Carolina, Inc. for adjustment of rates and)
charges and modifications to certain terms)
and conditions for the provision of)
water and sewer service.)
_____)

REBUTTAL TESTIMONY
OF
STEVEN LUBERTOZZI

1
2 **Q. WOULD YOU PLEASE STATE YOUR NAME, OCCUPATION AND BUSINESS**
3 **ADDRESS FOR THE RECORD?**

4 A. My name is Steven M. LubertoZZi. I am employed as the Chief Regulatory
5 Officer at Utilities, Inc., ("UI") through its shared services organization, 2335 Sanders
6 Road, Northbrook, Illinois 60062.

7 **Q. ARE YOU THE SAME STEVEN LUBERTOZZI THAT FILED DIRECT**
8 **TESTIMONY IN THIS DOCKET?**

9 A. Yes, I am.

10 **Q. PLEASE SUMMARIZE THE ISSUES YOU WILL BE ADDRESSING?**

11 A. The cost of debt used by ORS witness Webster, the overall revenue requirement if
12 the Commission were to except accept all of ORS' adjustments and United historical
13 financial performance.

14 **Q. WHAT ISSUES DO YOU HAVE WITH THE COST OF DEBT USED BY ORS**
15 **WITNESS HENRY WEBSTER?**

1 A. Mr. Webster uses a cost of debt rate of 6.58%, which is .02% below UI's actual
2 cost of debt. On July 19, 2006 UI entered into a Master Note Purchase Agreement,
3 wherein \$180,000,000 of collateral trust notes were issued at 6.58%. The additional
4 .02% represents costs to acquire the debt.

5 **Q. WHAT TYPES OF COSTS WERE INCURRED?**

6 A. In order to acquire the \$180,000,000 of debt at 6.58%, a rate that was in line with
7 market rates when it was acquired in 2006, UI had to engage lawyers, consultants, tax
8 advisors and incurred fees and costs. These costs incurred by UI are similar to costs a
9 homeowner would include to refinance a home mortgage. It would be completely
10 imprudent for any company to acquire any debt or issue any securities without the
11 assistance of lawyers, tax advisors and consultants.

12 **Q. ARE THESE COSTS SOMETIMES REFERRED TO AS FLOTATION COSTS?**

13 A. Often, the costs incurred by public traded companies to issue securities are
14 referred to as flotation costs. The costs at issue in this case, however, were incurred in
15 connection with a debt issuance and the term flotation cost does not fully reflect what
16 these costs really were and why they were incurred. I prefer to refer to as costs incurred
17 to acquire UI's long-term debt.

18 **Q. HOW MUCH DID UI INCUR TO ACQUIRE THE \$180,000,000 LONG-TERM**
19 **DEBT?**

20 A. UI incurred approximately \$1.3 million, which is less than 1% of the
21 \$180,000,000 offering. These costs are amortized over the term of the loan agreement,
22 which is 30 years, so UI expenses approximately forty-two thousand dollar per year.

1 **Q. HOW DID YOU ARRIVE AT 6.6% IF THE STATED INTEREST RATE IS**
2 **6.58%?**

3 A. UI makes semiannual interest payments in January and July of each year and each
4 payment is \$5,922,000, calculated below:

5
6
$$\$180,000,000 * 6.58\% * \frac{1}{2} = \$5,922,000$$

7
8 Therefore, UI pays annual interest expense of \$11.844 million.

9 UI incurred approximately \$1.3 million in fees and costs to acquire the
10 \$180,000,000. These fees are amortized over the life of the loan, which is 30 years or
11 \$42,000 of amortization expense per year.

12 I added the \$42,000 of amortization expense to the annual interest expense of
13 \$11.844 million which totals \$11.886 million of annual prudently incurred expense. The
14 calculation to obtain the 6.60% is provided below:

15
16 Annual expense:
$$\$180,000,000 * 6.58\% + \$42,000 = \$11,886,000$$

17 Annual cost rate:
$$\$11,886,000 / \$180,000,000 = 6.60\%$$

18
19 **Q. HAVE ALL OF UNITED'S SISTER COMPANIES OUTSIDE OF SOUTH**
20 **CAROLINA RECOVERED THESE COSTS?**

21 A. Yes, when filing rate cases for other UI operating companies we routinely include
22 the costs to acquire the \$180,000,000 and they have been routinely accepted by the

1 parties and included in rates by the Commissions in other jurisdictions (e.g., North
2 Carolina, Illinois, and Nevada).

3 **Q. IN YOUR OPINION WHAT IMPACT WOULD THE EXCLUSION OF THESE**
4 **COSTS HAVE?**

5 A. There will be several impacts. The first one would be that United would never
6 earn its authorized return, because the full cost of its debt will not be factored into rates.
7 Second, unrecovered costs could cause future interest rates available to UI (and other
8 utilities) to increase, because lending institutions will know that costs to acquire debt will
9 be at risk of not be recovered by customers.

10 **Q. IN YOUR OPINION SHOULD THE COSTS INCURRED TO ACQUIRE THE**
11 **\$180 MILLION OF LONG-TERM DEBT BE INCLUDED FOR RATEMAKING**
12 **PURPOSES?**

13 A. Absolutely, UI incurred these cost and there is no evidence to suggest that these
14 costs were imprudently incurred.

15 **Q. IF THE COMMISSION WERE TO ACCEPT ALL OF ORS' ADJUSTMENTS**
16 **AND USE THE MIDPOINT OF ITS ROE RANGE WHAT WOULD BE THE**
17 **RESULTING REVENUE REQUIREMENT?**

18 A. The resulting revenue requirement using all of ORS' adjustments is \$154,000.
19 However, for the reasons discussed in UI's rebuttal testimony, the Commission should
20 not accept the ORS's proposed adjustments.

21 **Q. PLEASE DISCUSS UNITED'S OVERALL FINANCIAL PERFORMANCE AND**
22 **HEALTH.**

A. As shown in PMA-2, Schedule 1R, Page 2 of 2 United financial performance for the past 13 years has been abysmal. The exhibit is provided in its entirety below:

Exhibit PMA-2
Schedule 1R
Page 2 of 2

United Utility Companies, Inc.
Revenues and Net Income for the years 2000 - 2012

<u>Year</u>	<u>Revenue</u>	<u>Net Income (Loss)</u>
2000	\$ 374,188	\$ (66,613)
2001	\$ 392,275	\$ (74,369)
2002	\$ 588,363	\$ (51,812)
2003	\$ 783,208	\$ 97,622
2004	\$ 863,061	\$ 22,334
2005	\$ 878,812	\$ (25,799)
2006	\$ 920,332	\$ (49,830)
2007	\$ 768,231	\$ (23,150)
2008	\$ 827,422	\$ (147,339)
2009	\$ 851,537	\$ (171,230)
2010	\$ 804,959	\$ 120,144
2011	\$ 790,549	\$ (145,814)
2012	\$ 890,215	\$ (78,327)

Source of Information: Company provided

United has lost money every year except 2010, 2004 and 2003. United only had net income in 2010 because of a gain on sale from divesting of two subdivisions. If not for that sale, United's net loss in 2010 would have been approximately \$34,000. While losing money is most years, United continued to deploy capital, more than \$3 million since 2000. If United was a standalone entity it would: (1) not be able to meet its

1 obligations as they come due, (2) not be able to attract debt without paying an excessively
2 high interest and (3) would not be able to attract equity.

3 **Q. HOW CAN THE COMMISSION SET UNITED'S RATE OF RETURN IN ORDER**
4 **THAT IT IS ALLOWED TO BE A FINANCIALLY STRONG UTILITY**
5 **OPERATING IN SOUTH CAROLINA?**

6 A. The Commission should set United's ROE at the top of the witness D'Ascendis'
7 range not the bottom of Dr. Carlisle's range as the ORS recommends. United had
8 multiple rate increases in the past. However, due to continue upward pressure on
9 expenses and continued capital deployment, United has negative free cash flow. As
10 shown by actual operating results, the regulatory process is inadequate by design.

11 **Q. PLEASE EXPLAIN WHAT YOU MEAN WHEN YOU SAY THAT THE**
12 **REGULATORY PROCESS IS INADEQUATE BY DESIGN.**

13 A. The parties in most rate cases in South Carolina spend excessive amounts of rate
14 case expense to litigate issues related to the cost of capital, particularly cost of equity. In
15 this case, we are arguing over whether United should be authorized an 8.86% ROE,
16 which would be the lowest ROE in recent history, or 11.45%, the top of Mr. D'Ascendis'
17 range. However, at the end of the day, those arguments are moot if the company has zero
18 chance of actually earning its authorized ROE. The Commission, United, ORS, and
19 customers would all be better off if rates were set at a level that allows a company to have
20 positive earning. However, this can only happen through the implementation of best
21 practices, which acknowledges the fact that a regulated water utility cannot earn its
22 authorized return. Without these United will be forced to file rate cases on a more
23 frequent basis, which only cause rates to increase.

1 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

2 A. Yes it does.